

STATE OF MONTANA

Public Employees' Retirement Board

A Component Unit of the State of Montana

Comprehensive Annual Financial Report



**For the Fiscal Year Ended
June 30, 2006**

Public Employees' Retirement System - Defined Benefit Retirement Plan

Judges' Retirement System

Highway Patrol Officers' Retirement System

Sheriffs' Retirement System

Game Wardens' and Peace Officers' Retirement System

Municipal Police Officers' Retirement System

Firefighters' Unified Retirement System

Volunteer Firefighters' Compensation Act

Public Employees' Retirement System - Defined Contribution Retirement Plan

Deferred Compensation (457) Plan

**Prepared By:
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Table of Contents

Introductory Section

Letter of Transmittal	5
Public Employees' Retirement Board	11
Montana Public Employee Retirement Administration Organizational Chart	12

Financial Section

Independent Auditor's Report	13
Management's Discussion & Analysis	15
Basic Financial Statements:	
<i>Statement of Fiduciary Net Assets -Pension Trust Funds</i>	30
<i>(The notes to the financial statements are an integral part of this statement)</i>	
<i>Statement of Changes in Fiduciary Net Assets -Pension Trust Funds</i>	32
<i>(The notes to the financial statements are an integral part of this statement)</i>	
<i>Notes to the Financial Statements</i>	34
Required Supplementary Information:	
Schedule of Funding Progress	78
Schedule of Employer Contributions and Other Contributing Entities	80
Notes to the Required Supplementary Information	82
Supporting Schedules:	
Schedule of Administrative Expenses	85
Schedule of Investment Expenses.....	86
Schedule of Consultants	87
Detail of Fiduciary Net Assets (PERS-DBRP, PERS-DBEd)	88
Detail of Changes in Fiduciary Net Assets (PERS-DBRP, PERS- DBEd)	89
Detail of Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and DC Disability)	90
Detail of Changes in Fiduciary Net Assets (PERS-DCRP, PERS-DCEd and DC Disability)	90

Investment Section

Report on Investment Activity	91
Rates of Return by Asset Class	92
Schedules of Asset Mix.....	96
Schedule of Largest Holdings	104
Investment Summary	108

Actuarial Section

Actuary's Certification.....	111
Summary of Actuarial Assumptions and Methods.....	113
Schedule of Active Member Valuation Data	116
Schedule of Active Member Composition	118
Schedule of Retirants and Beneficiaries Added to and Removed from Rolls.....	120
Solvency Test.....	122
Summary of Actuarial (Gain)/Loss by Source.....	124
Summary of Defined Benefit Plan Provisions	128

Statistical Section

Summary of Statistical Data.....	145
Changes in Net Assets.....	146
History of Actuarial Accrued Liabilities.....	153
Schedule of Fair Values by Type of Investment.....	156
Schedule of Contribution Rate History	161
Schedule of Benefit Expenses by Type.....	164
Schedule of Distributions Processed	168
Schedule of Retired Members by Type of Benefit.....	170
Distribution of Defined Benefit Recipients by Location.....	176
Average Benefit Payments.....	178
Schedule of Average Monthly Benefit Payments, All Retirees	186
Principal Participating Employers	188
Schedule of Participating Employers	192

Mission Statement of the PERB

The Montana Public Employees' Retirement Board will fiduciarily administer its retirement plans and trust funds, acting in the best interest of the members and beneficiaries.

Mission Statement of the MPERA

The Montana Public Employee Retirement Administration will efficiently provide quality benefits, education and service to help our plan members and beneficiaries achieve a quality retirement.

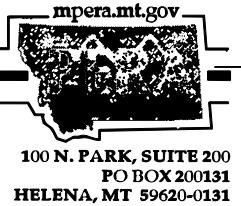
PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION



BRIAN SCHWEITZER
GOVERNOR

STATE OF MONTANA

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November 28, 2006

The Honorable Brian Schweitzer
Governor of Montana
Room 204, State Capitol
PO Box 200801
Helena, MT 59620-0801

Dear Governor Schweitzer:

The Public Employees' Retirement Board (PERB) and its staff, the Montana Public Employee Retirement Administration (MPERA), are pleased to submit this *Comprehensive Annual Financial Report* (CAFR) for the fiscal year ended June 30, 2006, in accordance with 19-2-407, Montana Code Annotated. The purpose of this letter is to introduce the basic financial statements and provide an analytical overview of the trust funds' financial activities.

The financial information presented in this report is the responsibility of the management of Montana Public Employee Retirement Administration and sufficient internal accounting controls exist to provide reasonable assurance regarding the safekeeping of assets and fair presentation of the financial statements, supporting schedules and statistical tables. This CAFR was prepared in conformance with the principles of governmental accounting and reporting set forth by the Governmental Accounting Standards Board, including the Management's Discussion and Analysis (MD&A). Defined benefit and defined contribution transactions are reported on the accrual basis of accounting. The Management Discussion & Analysis (MD&A) beginning on page 15, is a discussion, by management, of the financial position of the retirement plans. It provides an overview and analysis of the plans' basic financial statements. This letter of transmittal is intended to complement the MD&A and the two should be read in conjunction.

ORGANIZATIONAL STRUCTURE AND REPORT CONTENTS

The PERB is a discretely presented component unit Pension Trust Fund of the State of Montana financial reporting entity. For this reason, the financial statements contained in this report are also included in the State of Montana's *Comprehensive Annual Financial Report*. Fiduciary responsibility for the systems rests with the PERB, which consists of seven members, appointed by the Governor. The members are assigned five-year, staggered terms. The Board is required to approve a final budget before the beginning of the fiscal year. The management of MPERA develops the budget for all plans administered and presents it to the Board. As governed by statute, the Board's defined benefit administrative expenses may not exceed 1.5% of

INTRODUCTORY SECTION

the total defined benefit plan retirement benefits paid. Costs for the Board to administer the defined contribution plans are included as part of the administrative expenses of the plans. The budget is monitored throughout the year and quarterly updates are provided.

The Public Employees' Retirement Board administers ten separate retirement plans, each reported in this CAFR. They include the *Public Employees' Retirement System-Defined Benefit Retirement Plan* (in its 62nd year of operation) and *Public Employees' Retirement System-Defined Contribution Retirement Plan*, *Judges' Retirement System*, *Highway Patrol Officers' Retirement System*, *Sheriffs' Retirement System*, *Game Wardens' and Peace Officers' Retirement System*, *Municipal Police Officers' Retirement System*, *Firefighters' Unified Retirement System*, *Volunteer Firefighters' Compensation Act* and the *Deferred Compensation (457) Plan*. The CAFR is divided into the following five sections:

- an *Introductory Section*, which contains the table of contents, this letter of transmittal and administrative organization;
- a *Financial Section*, which contains the report of the Independent Auditors, the Management's Discussion and Analysis, the financial statements of the PERB, the notes to the financial statements, certain required supplementary information and supporting schedules of administrative expenses, investment expenses and payments to consultants;
- an *Investment Section*, which contains a report on investment activity, investment policies, investment results and various investment schedules;
- an *Actuarial Section*, which contains the Actuary's Certification Letter and the results of the latest actuarial valuation; and,
- a *Statistical Section*, which includes significant data pertaining to the plans.

The pages that follow report the facts and figures that are the result of dedicated work, new initiatives, improved processes and continuing efforts made to meet the needs of our customers. We trust that you and the members of the plans will find this CAFR helpful in understanding the retirement plans.

ECONOMIC CONDITION AND OUTLOOK

The economic outlook of the plans is based primarily upon investment earnings. For 2006, the PERS-DBRP experienced a 9.07 percent fair value rate of return, for the last three years an average annualized rate of return of 10.19 percent and for the last five years an average annualized rate of return of 5.76 percent. The plans are required by law to be maintained on an actuarially sound basis thus protecting participants' future benefits.

The PERB contracts with consultants for professional services, which are essential to the effective and efficient operation of the plans. A listing of consultants the PERB has contracted with can be found on page 87.

The investments of the pension trust funds are governed, primarily, by an investment standard known as the "prudent expert principle." The prudent expert principle is constitutionally and statutorily mandated and establishes a standard for all fiduciaries, which includes

anyone having authority with respect to the pension trusts. The prudent expert principle states that fiduciaries will discharge their duties solely in the interest of the trust funds' participants and beneficiaries and with the degree of diligence, care and skill which prudent experts would ordinarily exercise under similar circumstances in a like position. By following the prudent expert principle and permitting further diversification of investments within a fund, the fund may reduce overall risk and increase returns. The prudent expert principle permits the PERB to establish an investment policy based upon certain investment criteria and allows for the delegation of investment authority to the Board of Investments (BOI), Department of Commerce. The statement of investment policy outlines the responsibility for the investment of the funds and the degree of risk that is deemed appropriate for the trust funds. Investment officers are to execute the investment policy in accordance with statutory authority, the PERB's policy and their respective guidelines, but are to use full discretion within the policy and guidelines. A summary of the asset allocations can be found in the *Investment Section* of this annual report.

Pension trust funds are well-funded when there is enough money in reserve to meet all expected future obligations to participants. The PERB's funding objective is to meet long-term benefit promises through contributions that remain approximately level as a percent of member payroll. The greater the level of funding, the larger the ratio of assets accumulated to the actuarial accrued liability and the greater the level of investment potential. The advantage of a well-funded plan is participants can see assets that are committed to the payment of benefits. A detailed discussion of funding is provided in the *Actuarial Section* of this annual report beginning on page 111. More information has been added to the *Statistical Section* of this annual report including the five objectives according to GASB 44: financial trends, revenue capacity, debt capacity, demographic and economic information and operating information.

The previous bear market had a negative affect on earnings and although recovery has been slow, we anticipate that over the long-term the earning rates will continue to meet the actuarial assumed rate of 8 percent. Current member benefits will not be changed, although the legislature will review the funding and assure the plans are funded on an actuarially sound basis. Based on the report of our actuary for July 1, 2006, one of the eight defined benefit plans had surplus funding and three of the eight defined benefit plans (PERS, GWPORS and SRS) have an actuarial liability that does not amortize over the required 30 years. Legislation seeking to increase employer contributions in those three systems was not approved by the 2005 Legislature, nor the Special Session. MPERA is hopeful that the 2007 Legislature will address the plans' funding needs.

The PERS-DCRP was implemented July 1, 2002. New hires of the PERS have the option of choosing participation in either the defined benefit retirement plan (DBRP) or the defined contribution retirement plan (DCRP). University employees also have a third option of joining the Optional Retirement Program (ORP) administered by the Teachers Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF New York, NY).

All new hires are offered Plan Choice Educational workshops funded by a percentage of em-

INTRODUCTORY SECTION

ployer contributions. Education to our members and employers is a top priority. We continue to add workshops and member services through our website.

The web reporting systems take advantage of advanced technology and result in more accurate reporting and more timely deposits to participants' accounts. All payrolls must be reported within five working days of each payday. These web reporting systems continue to be enhanced as we receive comments recommending improvements from employers and staff and to assure compatibility with software upgrades.

The MPERA web page was recently redesigned to comply with the state standard for web pages. The new look will make it easier for users to find desired topics and extract necessary information from the web site. Our web site includes descriptions and information on all plans administered by the PERB; the organization of the PERB along with the goals, objectives and how to contact the PERB; meeting dates and times; administrative rules; access to the employer reporting system; frequently asked questions; and publications including newsletters, member and employer handbooks, actuary valuations, and this *Comprehensive Annual Financial Report* (CAFR).

CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Montana Public Employees' Retirement Board for its comprehensive annual financial report for the fiscal year ended June 30, 2005. This was the eighth consecutive year that the Montana Public Employees' Retirement Board has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government entity must publish an easily readable and efficiently organized *Comprehensive Annual Financial Report*. This report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. We believe our current *Comprehensive Annual Financial Report* continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

ACKNOWLEDGEMENTS

The compilation of this report reflects the efforts of the fiscal services bureau accounting staff of the Montana Public Employee Retirement Administration. This report is intended to provide complete and reliable information to facilitate the management decision process, as a means of determining compliance with legal provisions, and as a means of determining responsible stewardship of the funds of the plans. As in the past, MPERA received an unqualified opinion from our independent auditors on the financial statements included in this report. This opinion provides assurance that the financial statements can be relied upon. The independent auditor's opinion letter can be found on page 13.

INTRODUCTORY SECTION

The reporting employers of each retirement system form the link between the plans and the members. Their cooperation contributes significantly to the success of the plans. We hope the employers and their employees find this report informative.

We would like to take this opportunity to express our gratitude to the staff, the advisors and the many people who have worked so diligently to assure the successful operation of the plans.

Respectfully submitted,



Roxanne Minnehan, Executive Director
Montana Public Employee Retirement Administration



Carole Carey, President
Public Employees' Retirement Board

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Montana Public Employees' Retirement Board

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

Public Employees' Retirement Board

A Component Unit of the State of Montana



Photo taken by Kim Flatow

Back Row: Jay Klawon, Terrence Smith, Troy McGee and John Paull,
Front Row: Carole Carey, Robert Griffith, and Elizabeth Nedrow.

Carole Carey, President
Ekalaka
Active Public Employee
Clerk of District Court
Carter County
Term Expires 3/31/2007

Troy McGee
Helena
PERS Retired Member
Term Expires 3/31/2008

Terrence Smith
Bozeman
PERS-DCRP Active Public
Employee
Financial Officer
Big Sky Water & Sewer
District
Term Expires 3/31/2009

John Paull, Vice President
Butte
Active Public Employee
Fireman
Term Expires 3/31/2010

Robert Griffith
Helena
Member at Large
Term Expires 3/31/2008

N. Jay Klawon
Hamilton
Investment Experience
Investment Representative
Edward Jones
Term Expires 3/31/2009

Elizabeth Nedrow
Billings
Member at Large
Attorney
Holland & Hart
Term Expires 3/31/2011

INTRODUCTORY SECTION

Public Employees' Retirement Board

A Component Unit of the State of Montana

MPERA Organizational Chart

